

Message Text

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PAGE 01 LONDON 07357 01 OF 03 041852Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 SP-02 AID-05
EB-07 NSC-05 EPG-02 SS-15 STR-04 OMB-01 CEA-01
CIAE-00 FRB-01 INR-07 NSAE-00 XMB-04 OPIC-06
LAB-04 SIL-01 USIE-00 FEAE-00 IGA-02 DODE-00
PA-02 PRS-01 SSO-00 NSCE-00 INRE-00 AGRE-00
EURE-00 /115 W

-----041907Z 000362 /41

O R 041756Z MAY 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 3477
TREASURY DEPT WASHDC IMMEDIATE
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY DUBLIN
AMEMBASSY NEW DELHI
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY TOKYO
AMCONSUL BELFAST
AMCONSUL EDINBURGH
USMISSION EC BRUSSELS
USMISSION OECD PARIS
USDEL MTN GENEVA
USDOC WASHDC

UNCLAS SECTION 01 OF 03 LONDON 07357

DEPARTMENT PASS FEDERAL RESERVE BOARD

TREASURY FOR DONALD E. SYVRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: ECONOMIC DEVELOPMENTS FOR PERIOD APRIL 28-.MAY 4

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PAGE 02 LONDON 07357 01 OF 03 041852Z

SUMMARY: BUSINESS SURVEYS POINT TO HIGHER LEVELS OF INVESTMENT LATER IN 1977 AND IN 1978. IN ITS FIRST YEAR OF OPERATION THE NATIONAL ENTERPRISE BOARD MADE A PRE-TAX PROFIT OF 51.3 MILLION POUNDS. SHORT-TERM INTEREST RATES FELL SHARPLY TO LEVELS NOT SEEN SINCE 1973 WHILE BRITAIN'S FOREIGN EXCHANGE RESERVES ROSE ABOVE 10 BILLION DOLLARS. END SUMMARY.

1. FINANCIAL MARKETS SAW FURTHER FALLS IN INTEREST RATES THIS WEEK. SHORT-TERM INTEREST RATES FELL ON THE ORDER OF 1/2 PERCENT OVER THE WEEK, WHILE DECLINES IN LONG YIELDS WERE MORE MODEST. ON THE ORDER OF 1/4 PERCENT.

THE MAJOR CLEARING BANKS REDUCED THEIR BASE LENDING RATES FROM 9 TO 8 1/2 PERCENT. AND THEIR RATE ON 7-DAY BRANCH DEPOSITS FROM 4.1/2 TO 4 PERCENT. BASE LENDING RATES ARE NOW LOWER THAN THEY HAVE BEEN SINCE AUGUST 1973. BANKS HAVE INDICATED, HOWEVER. THAT THE DROP IN RATES HAS NOT ENCOURAGED A SIGNIFICANT INCREASE IN INDUSTRIAL BORROWING. THIS MIGHT SIMPLY REFLECT THE DEFERRAL OF BORROWING IN ANTICIPATION OF REDUCED INTEREST RATES

THE BANK OF ENGLAND REDUCED ITS MINIMUM LENDING RATE (MLR) L/2 PERCENT TO 8-1/4 PERCENT ON APRIL 29. IN SO SETTING THE RATE. THE BANK OVERRODE THE TREASURY BILL RATE-BASED FORMULA WHICH WOULD HAVE SPECIFIED AN MLR OF 8 PERCENT. FURTHER DECLINES IN THE TREASURY BILL RATE OVER THIS WEEK INDICATE THAT AN ADDITIONAL CUT IN THE MLR IS LIKELY AT FRIDAY S AUCTION IF THE FORMULA IS FOLLOWED.

2. U.K. FOREIGN EXCHANGE RESERVES ROSE \$512 MILLION TO STAND AT A RECORD LEVEL OF \$10.13 BILLION. (SEE LONDON 7228.)

3. CBI BUSINESS SURVEY. IN AN OTHERWISE RATHER FEATURELESS QUARTERLY SURVEY OF 1721 FIRMS. THE CONFEDERATION OF BRITISH INDUSTRY (CBI) REPORTS THE LARGEST FAVORABLE UNCLASSIFIED

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PAGE 03 LONDON 07357 01 OF 03 041852Z

BALANCE OF REPLIES ON INVESTMENT INTENTIONS OVER THE NEXT YEAR SINCE 1958. CBI CONCLUDES "IF THE PAST RELATIONSHIPS BETWEEN OUR SURVEY DATA AND OFFICIAL STATISTICS OF CAPITAL EXPENDITURE HOLD, THE VOLUME OF MANUFACTURING INVESTMENT COULD BE 20 PERCENT HIGHER IN THE YEAR ENDING SEPTEMBER 1978 THAN IN THE YEAR ENDING SEPTEMBER 1977."

IN OTHER AREAS. THE SURVEY RESULTS INCLUDE:

- A SLIGHT LENGTHENING IN BACKLOGS
- SLIGHTLY IMPROVED INTENTIONS TO TAKE ON LABOR
- NO INCREASE IN INVENTORIES OVER THE NEXT FOUR MONTHS
- AN EMERGING CONSTRAINT IN THE AREA OF

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PAGE 01 LONDON 07357 02 OF 03 041856Z
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PRS-01 IGA-02 FEAE-00 SSO-00 NSCE-00 INRE-00
EURE-00 /115 W
-----041914Z 000404 /42

O R 041756Z MAY 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 3478
TREASURY DEPT WASHDC IMMEDIATE
INFO AMEMBASSY BONN
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UNCLAS SECTION 02 OF 03 LONDON 07357

SKILLED LABOR
- VIRTUALLY NO FINANCIAL CONSTRAINT ON FUTURE
INVESTMENT
- SLIGHTLY LOWER LEVELS OF OPTIMISM ON EXPORT
PROSPECTS OVER THE COMING YEAR.
THE CBI SURVEY REINFORCES THE FINDINGS REPORTED BY
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PAGE 02 LONDON 07357 02 OF 03 041856Z

THE FINANCIAL TIMES (FT) (SEE FOLLOWING PARAGRAPH.) IN
COMMENTING ON THE CBI FINDINGS, THE FT CONTRASTS THEIR
RELATIVELY OPTIMISTIC RESULTS WITH THE RECENT DISAPPOINT-

ING PERFORMANCE OF THE ECONOMY. IT POINTS TO A BELIEF THAT THE WORST OF THE DOWNWARD ECONOMIC ADJUSTMENT, PARTICULARLY IN REAL WAGES, MAY BE OVER. THIS TOGETHER WITH A HEALTHY BALANCE OF PAYMENTS MAY HAVE CREATED A CONFIDENCE THAT U.K. BUSINESS IS "IN CONTROL OF THEIR OWN FATE RATHER THAN A SLAVE TO OUTSIDE TRENDS."

4. FT BUSINESS SURVEY. THE FINANCIAL TIMES MONTHLY SURVEY OF BUSINESS OPINION REFLECTS RISING CONFIDENCE ABOUT THE GENERAL ECONOMIC CLIMATE. BETWEEN JANUARY AND THE LATEST SURVEY IN APRIL, THE PERCENTAGE OF RESPONDENTS EXPRESSING CONFIDENCE ABOUT THEIR FIRM'S PROSPECTS ROSE FROM 29 TO 43 PERCENT WHILE THOSE EXPRESSING PESSIMISM DECLINED FROM 43 TO 10 PERCENT. THIS MARKED SHIFT COINCIDES WITH IMPROVING EXPECTATIONS ABOUT EARNINGS AND INVESTMENT. BOTH THE TRENDS IN EXPORT PROSPECTS AND NEW ORDERS ARE REPORTED TO BE STRONGLY IMPROVED. REFLECTING THIS STRENGTH FIRMS ARE INTENDING TO INCREASE STOCKS OF BOTH RAW MATERIALS AND FINISHED GOODS.

ON THE SUPPLY SIDE, POTENTIAL PROBLEMS ARE BEGINNING TO CROP UP AMONG MANAGEMENT PERSONNEL AND SKILLED LABOR ALTHOUGH NEITHER OF THESE FACTORS WAS A PROBLEM FOR MORE THAN A QUARTER OF RESPONDENTS. THE SURVEY RESULTS DO NOT POINT TO AN EARLY RETURN TO LARGE-SCALE HIRING. INVESTMENT INTENTIONS ARE ALSO STRENGTHENING WITH 58 PERCENT OF RESPONDENTS PLANNING TO INCREASE THE VOLUME OF INVESTMENT OVER THE NEXT YEAR COMPARED WITH 42 PERCENT IN JANUARY. THE MEDIAN ANTICIPATED UNIT COST INCREASE OVER THE NEXT YEAR REMAINS IN THE RANGE OF 13.5 PERCENT. REFLECTING THE APPARENT IMPACT OF INCOMES POLICY, THE MEDIAN RISE IN UNIT LABOR COSTS IS PUT AT 10.7 PERCENT. FINALLY, PROFIT MARGINS ARE EXPECTED TO WIDEN BY 39 PERCENT OF THE SURVEYED FIRMS AND NARROW BY 12 PERCENT. THE BAL-

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PAGE 03 LONDON 07357 02 OF 03 041856Z

ANCE ON OVERALL EARNINGS IS EVEN MORE FAVORABLE -- 56 PERCENT EXPECT BETTER EARNINGS WHILE 11 PERCENT DO NOT.

THE RELATIVELY ROSY FUTURE PRESENTED BY THESE SURVEY RESULTS HAS NOT AS YET BEEN BORNE OUT, PARTICULARLY IN THE AREA OF INVESTMENT. IT IS TRUE, HOWEVER, THAT CORPORATE EARNINGS REBOUNDED STRONGLY IN 1976 ALBEIT FROM DEPRESSED LEVELS AND ARE STILL SHOWING SIGNS OF CONSIDERABLE STRENGTH.

5. NATIONAL ENTERPRISE BOARD. IN ITS FIRST ANNUAL REPORT, THE STATE-OWNED NATIONAL ENTERPRISE BOARD (NEB) SHOWED A PRE-TAX PROFIT OF 51.3 MILLION POUNDS ON SALES OF 2.8 BILLION POUNDS. THE NEB FUNCTIONS INTER ALIA AS A HOLDING COMPANY FOR THE CORPORATE ASSETS OF SEVEN FIRMS ACQUIRED BY HMG TO PREVENT THEIR FINANCIAL COLLAPSE.

FOREMOST AMONG THESE ARE BRITISH LEYLAND, ROLLS ROYCE, AND ALFRED HERBERT (THE LARGEST UK FOUNDRY). THE NEB HAS SINCE ACQUIRED INTERESTS IN A FURTHER 16 FIRMS. THESE ARE RELATIVELY SMALL FIRMS WHOSE EQUITY BASE IS GENERALLY BELOW 3 MILLION POUNDS. IN ITS VARIOUS ROLES AS MERCHANT BANKER, HOLDING COMPANY. AND MANAGEMENT CONSULTANT, THE NEB HAS FUNCTIONED WITH A TOTAL STAFF OF ONLY 50 PEOPLE INCLUDING 20 PROFESSIONALS DRAWN FROM PRIVATE INDUSTRY. IN A PRESS CONFERENCE, NEB CHAIRMAN, LORD RYDER. SAID THAT THE NEB WAS FILLING A VOID BY PROVIDING CAPITAL TO ENLARGE THE EQUITY BASE OF SMALL FIRMS WITH BRIGHT PROSPECTS. HE ESTIMATED THAT THE NEB'S EQUITY HOLDINGS WOULD GROW FROM THEIR PRESENT LEVEL OF 16 SMALL FIRMS TO PERHAPS 50 TO 70 FIRMS BY THE END OF 1977.

6. THE POUND HAD A QUIET WEEK. AND WAS FIRM IN SPOT QUOTATIONS DESPITE LAST FRIDAY'S CUT IN MLR. THERE WAS SMALL-SCALE SPOT ACTIVITY, WITH SOME PROFESSIONAL DEALING IN FORWARDS AS U.K. INTEREST RATES FELL AND U.S. RATES TIGHTENED. MOST ACTION, HOWEVER, WAS IN DOLLAR/DM AND UNCLASSIFIED

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PAGE 04 LONDON 07357 02 OF 03 041856Z

DOLLAR/GUILDER THERE ARE STILL RUMORS OF A GUILDER REVALUATION.

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PAGE 01 LONDON 07357 03 OF 03 041905Z
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XMB-04 OPIC-06 LAB-04 SIL-01 USIE-00 DODE-00
PA-02 PRS-01 IGA-02 FEAE-00 SSO-00 NSCE-00 INRE-00
/115 W

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O R 041756Z MAY 77
FM AMEMBASSY LONDON

TO SECSTATE WASHDC IMMEDIATE 3479
 TREASURY DEPT WASHDC IMMEDIATE
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UNCLAS SECTION 03 OF 03 LONDON 07357

7. EXCHANGE RATE AND GOLD EFFECTIVE
 EXCHANGE RATE

DATE	EXCHANGE (DEC. 1971 RATE (\$ EQUALS 100)	GOLD (\$)
4/27	1.7200 61.7	147-5/8

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PAGE 02 LONDON 07357 03 OF 03 041905Z

4/28	1.7193 61.6	146-1/8
4/29	1.7194 61.6	147-3/8
5/2	1.7196 61.7	148-7/8
5/3	1.7194 61.7	147-7/8

CHANGE 4/26-5/3 UP 0.000L DOWN 0.1 UP 3/4

8. FORWARD DISCOUNT ON STERLING

DATE	0.60	1.70	3.60
4/27	0.60	1.70	3.60
4/28	0.50	1.58	3.37
4/29	0.42	1.47	3.12
5/2	0.42	1.18	2.57
5/3	0.40	1.18	2.62

CHANGE 4/26.5/3 NAR. 0.18 NAR. 0.52 NAR. 0.98
 (ALL FIGURES IN CENTS)

9. EURODOLLAR INTEREST RATES

DATE	1 MONTH	3 MONTHS	6 MONTHS
4/27	4-7/8	5-1/4	5-1/2
4/28	5	5-1/4	5-1/2
4/29	5	5-1/4	5-1/2
5/2	5 1/4	5-3/8	5-3/4

5/3 5-3/8 5-3/8 5-7/8
CHANGE 4/26-5/3 UP 3/8 UP 1/8 UP 1/4

10. THREE-MONTH LONDON INTERBANK - EURODOLLAR INTEREST
RATE DIFFERENTIAL

DATE	
4/27	2-31/32
4/28	2-25/32
4/29	2-23/32
5/2	2-7/16
5/3	2-3/8

CHANGE 4/26-5/3 NARROWED 5/8

11. STERLING CERTIFICATES OF DEPOSIT

- DATE 1 MONTH 3 MONTHS 6 MONTHS

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PAGE 03 LONDON 07357 03 OF 03 041905Z

4/27	8-3/16	8	8-15/64
4/28	8-5/32	7-7/8	8-1/8
4/29	7-15/16	7-23/32	8
5/2	7-53/64	7-11/16	8
5/3	7-11/16	7-5/8	8

CHANGE 4/26-5/3 DOWN 17/32 DOWN 1/2 DOWN 5/16

12. THE MINIMUM LENDING RATE WAS SET AT 8.1/4 PERCENT, DOWN FROM LAST WEEK'S 8-3/4 PERCENT, BY THE BANK OF ENGLAND. THE BANK IN SO SETTING THE RATE OVERRODE THE TREASURY BILL RATE-BASED FORMULA WHICH IMPLIED AN MLR OF 8 PERCENT. THE AVERAGE TREASURY BILL RATE FELL 0.5043 PERCENT TO 7.4973 PERCENT AT THE APRIL 29 AUCTION, AS 1,022.06 MILLION POUNDS IN BIDS WERE RECEIVED FOR THE 350 MILLION POUNDS TENDERED. THIS WEEK 350 MILLION POUNDS WILL BE OFFERED AS 300 MILLION POUNDS MATURE.

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Message Attributes

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Decaption Note:
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Disposition Approved on Date:
Disposition Case Number: n/a
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